

ST 03-0002-GIL 01/03/2003 SERVICE OCCUPATION TAX

If tangible personal property is transferred incident to sales of service, this will result in either Service Occupation Tax liability or Use Tax liability for the servicemen depending upon his activities. See 86 Ill. Adm. Code 140.101. (This is a GIL).

January 3, 2003

Dear Xxxxx:

This letter is in response to your letter dated September 18, 2002. The nature of your letter and the information you have provided require that we respond with a General Information Letter, which is designed to provide general information, is not a statement of Department policy and is not binding on the Department. See 2 Ill. Adm. Code 1200.120 subsections (b) and (c), which can be found at <http://www.revenue.state.il.us/Laws/regs/part1200/>.

In your letter, you have stated and made inquiry as follows:

Every so often we are invoiced for repair or installation material and labor in regards to a piece of our equipment. We are not a manufacturer - we are primarily a wholesaler of specialty metal and fiberglass products; however, we do light spot fabrication such as welding and cutting to meet our customer's demands. Recently, we were invoiced for labor and material for inspection, removal, and installation of a new valve assembly on our shear, which is a machine we use to cut pieces of perforated metals to size for our customers. The amount of the labor and material are almost equal in price. We were not charged any sales tax on this invoice by the repairer/installer. I called the Illinois Department of Revenue and spoke with Pat. She said that neither the materials nor labor for a repair or an installation would be taxable. She could not point me to any statute or regulation that I could refer to, so I asked if anyone could get me that information. She had me leave a voicemail for PERSON. A few days later I did not hear back from PERSON, so I tried to call. I reached a representative named Karen. She didn't think PERSON was in, but asked me to discuss the situation with her. Again, she told me neither the labor nor materials for an installation or a repair would be taxable. She said I would give the repairer an ST587 for the materials. We have not given the repairer a ST587 to date. Further, she said if the repairer/installer did not charge us tax, if we were audited, we would not be liable for penalty or interest on the invoice. She said that the auditor would go after the repairer/installer if it was found taxable. I again asked for a statute or regulation I could refer to, but she said it is not her job to find statutes. She then referred me to write to the Legal Department for any decision or statute/regulation reference.

Can you please let me know if we owe any tax on the invoice above? Also, can you confirm that we would not be liable for tax, penalty, or interest if a repairer/installer does not bill us tax on the invoice? Lastly, can you please refer me to any statute, regulation,

or guidance that states our liability for tax on a repair/install for our equipment? I want to make sure we are in compliance for this invoice as well as any other future invoices.

If you have any questions or need additional information to process this request, please do not hesitate to contact me. I appreciate your assistance with this matter.

DEPARTMENT'S RESPONSE:

Service and repair situations in Illinois can be some of the most confusing transactions from a sales or service tax compliance perspective. This is probably why your inquiry was finally directed to our office. We hope the following general information will assist you.

Illinois Retailers' Occupation and Use Taxes do not apply to sales of service that do not involve the transfer of tangible personal property to customers. However, if tangible personal property is transferred incident to sales of service, this will result in either Service Occupation Tax liability or Use Tax liability for the servicemen depending upon his activities. For your general information we are enclosing copies of 86 Ill. Adm. Code 140.101 through 140.109 regarding sales of service and Service Occupation Tax.

Under the Service Occupation Tax Act, businesses providing services (i.e. servicemen) are taxed on tangible personal property transferred as an incident to sales of service. See the enclosed copy of 86 Ill. Adm. Code 140.101. The purchase of tangible personal property that is transferred to the service customer may result in either Service Occupation Tax liability or Use Tax liability for the servicemen depending upon his activities. The serviceman's liability may be calculated in one of four ways: (1) separately stated selling price of tangible personal property transferred incident to service; (2) 50% of the servicemen's entire bill; (3) Service Occupation Tax on the servicemen's cost price if the servicemen are registered de minimis servicemen; or (4) Use Tax on the servicemen's cost price if the servicemen are de minimis and are not otherwise required to be registered under Section 2a of the Retailers' Occupation Tax Act.

Using the first method, servicemen may separately state the selling price of each item transferred as a result of the sale of service. The tax is then calculated on the separately stated selling price of the tangible personal property transferred. If the servicemen do not separately state the selling price of the tangible personal property transferred, they must use 50% of the entire bill to the service customer as the tax base. Both of the above methods provide that in no event may the tax base be less than the servicemen's cost price of the tangible personal property transferred. See the enclosed copy of 86 Ill. Adm. Code 140.106. These methods result in the customer incurring a Service Use Tax liability. See the enclosed copy of 86 Ill. Adm. Code 160.101.

The third way servicemen may account for their tax liability only applies to de minimis servicemen who have either chosen to be registered or are required to be registered because they incur Retailers' Occupation Tax liability with respect to a portion of their business. See the enclosed copy of 86 Ill. Adm. Code 140.109. Servicemen may qualify as de minimis if they determine that the annual aggregate cost price of tangible personal property transferred as an incident of the sale of service is less than 35% of the total annual gross receipts from service transactions (75% in the case of pharmacists and persons engaged in graphics arts production). Servicemen no longer have the option of determining whether they are de minimis using a transaction by transaction basis. Registered de minimis servicemen are authorized to pay Service Occupation Tax (which includes local taxes) based upon their cost price of tangible personal property transferred incident to the sale of service. Such servicemen should give suppliers resale certificates and remit Service Occupation

Tax using the Service Occupation Tax rates for their locations. This method also results in the customer incurring a Service Use Tax liability.

The final method of determining tax liability may be used by de minimis servicemen that are not otherwise required to be registered under Section 2a of the Retailers' Occupation Tax Act. Such de minimis servicemen handle their tax liability by paying Use Tax to their suppliers. If their suppliers are not registered to collect and remit tax, the servicemen must register, self-assess and remit Use Tax to the Department. The servicemen are considered to be the end-users of the tangible personal property transferred incident to service. Consequently, they are not authorized to collect a "tax" from the service customers. See the enclosed copy of 86 Ill. Adm. Code 140.108. Under this method, the customer incurs no Service Use Tax liability.

Please note that servicemen who account for their tax liability under the first through third methods above, are not required to separately state the tax on their bills unless so requested by their service customers. See subsection (e) of 86 Ill. Adm. Code 140.106 and subsection (a)(4) of 86 Ill. Adm. Code 140.109. For this reason, it is difficult to determine if a serviceman has collected tax when no tax is stated on the service customer's bill. For your general information, please see subsection (g) of Section 160.101 (copy enclosed) that describes the situation when a service customer receives an invoice from a serviceman that does not contain a separate charge for tax:

"If a serviceman incurring Service Occupation Tax liability is required or authorized to collect the Service Use Tax (see Section 160.115 for further information), the purchaser must pay the tax to the serviceman. The Department will presume that a serviceman is required or authorized to collect the Service Use Tax if he bills tax to the service customer. Stated conversely, if an invoice from a serviceman does not show the tax, the Department will presume that the serviceman is either registered and has included the Service Use Tax in the selling price of the tangible personal property transferred or is a de minimis serviceman incurring a Use Tax liability, in which case there is no collection obligation on the part of the purchaser. This presumption will be overcome only where the Department has evidence that the serviceman and/or the service customer were both aware that the proper tax due was the Service Use Tax and that no action was taken to remit the Service Use Tax by either party to the Transaction. A serviceman need not remit that part of any Service Use Tax collected by him to the extent that he is required to pay and does pay Service Occupation Tax to the Department on his sales of service involving the transfer by him of the same property, provided, however, that the amount paid to the Department is equal to or exceeds the amount collected from the service customer."

Please note that, even though your letter states that your company is not a manufacturer, some of the uses of your equipment could possibly qualify as manufacturing for purposes of the manufacturing machinery and equipment exemption. We would need additional information to make that determination. We urge you to review the enclosed copy of 86 Ill. Adm. Code 130.330. Under the Retailers' Occupation Tax Act and Service Occupation Tax Act, the manufacturing machinery and equipment exemption is available for machinery and equipment used primarily (over 50% of the time) in the manufacturing or assembling of tangible personal property for wholesale or retail sale or lease. A retailer of machinery and equipment must obtain proper documentation in the form of an exemption certificate from the purchaser in order to claim this exemption. See subsection (g) of 86 Ill. Adm. Code 130.330.

I hope this information is helpful. The Department of Revenue maintains a website, which can be accessed at www.revenue.state.il.us. If you have further questions related to the Illinois sales tax laws, please contact the Department's Taxpayer Information Division at (217) 782-3336.

If you are not under audit and you wish to obtain a binding Private Letter Ruling regarding your factual situation, please submit all of the information set out in items 1 through 8 of Section 1200.110(b) described above.

Very truly yours,

Terry D. Charlton
Associate Counsel

TDC:msk
Enc.